



THE CONSTITUTIONALITY OF RETROACTIVE TAX LEGISLATION

by

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Annexure G

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The constitutionality of retroactive tax legislation

Summary

In the constitutional dispensation in South Africa, the powers of the legislature flow from the constitution. Such powers must be exercised in a manner that aligns with the constitution. Consequently, retroactive taxation legislation must conform to the constitution. This mini-dissertation discusses the question whether retroactive taxation legislation is constitutionally valid. The constitutional validity of retroactive taxation legislation is tested through a discussion of the rule of law, the right to property and foreign law.

The rule of law is a foundational value of the constitution and as such, it must be reflected in legislative measures. Whether the legislature is upholding the rule of law when enacting retroactive tax legislation is an issue that is discussed in the mini-dissertation. In addition, the rulings of the judiciary must also be informed by the rule of law, the role of the judiciary is also discussed. This study also discusses whether retroactive tax legislation constitutes a deprivation of property of the taxpayers. Furthermore, this study discusses whether retroactive tax legislation amounts to an arbitrary deprivation of property. The limitations clause is also discussed.

This research also details the approach of foreign jurisdictions to retroactive tax legislation; this is done because the Constitution directs that the courts may consider foreign law when interpreting the Bill of Rights. Retroactive tax legislation is not prohibited in any of the considered foreign jurisdictions. Furthermore, this study finds that South Africa is distinguishable from the foreign jurisdictions based on the limitations clause of the constitution. Lastly, the writer provides a short summary and conclusion of this research.

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Chapter 1: Background

1.1 Introduction

With the enactment of retroactive tax legislation comes the possibility of new financial obligations being placed on taxpayers. These would be obligations which did not exist at the time of the conclusion of certain transactions by the taxpayers. Retroactive legislation is defined as legislation that functions from a time prior to its enactment.¹ It is different from retrospective legislation which is defined as legislation that is prospective in nature but attaches new results for past events.² The retroactive imposition of new financial obligations on taxpayers may arise as a result of a decision of the legislature to retroactively close a loophole in fiscal legislation. In addition to closing an identified loophole in the legislation, retroactive tax legislation may be imposed to counter tax avoidance.³ The question to be asked is whether retroactive tax legislation is justifiable in an open and democratic South Africa which is founded on values which include the rule of law and the supremacy of the Constitution.⁴

The supremacy of the Constitution means, among other things, that the legislature must not enact legislation that undermines the Constitution because the legislature is bound by the Constitution.⁵ Legislation that is enacted must therefore be in conformity with the Constitution. Moreover, the judiciary is empowered to declare any law or conduct that is in conflict with the provisions contained in the Constitution unconstitutional to the extent of its inconsistency.⁶ The powers granted to the judiciary are clearly safe guards that are supposed to ensure that legislation that does not pass the constitutionality test does not prevail where such statute has been brought before the judiciary. The purpose of

¹ Driedger, E.A. 1978. Statutes: retroactive retrospective reflections. *Canadian Bar Review*, 56: 268.

² Driedger, E.A. 1978. Statutes: retroactive retrospective reflections, 56: 26.

³For example, the Income Tax Act 129 of 1991 which amended the definition of 'person' in the Act to include a trust and the amendment was given retrospective application. The Taxation Laws Amendment Act 8 of 2007 is another example, it was used by the legislature to amend the Income Tax Act 58 of 1962 by removing the exemption on shares issued from a share premium account, with retrospective effect.

⁴ Section 1 (c) of the Constitution of the Republic of South Africa.

⁵ Section 2 of the Constitution.

⁶ Section 172 of the Constitution.

this study is to evaluate the constitutionality of the imposition of taxation legislation with retroactive effect. This will be done through a discussion of the rule of law, the right to property and the approach in foreign jurisdictions.

1.2 Problem Statement

The legislature does from time to time enact taxation legislation that has retroactive effect and this has adverse consequences to taxpayers in certain instances. In effect, taxpayers may be faced with obligations to pay certain amounts to the fiscus that were not payable at the time of the conclusion of certain legal acts. The rule of law requires, *inter alia*, that taxpayers must be able to ascertain what the law is, and that taxpayers must be able to place reliance on the law as it stands.⁷ Furthermore, the right to property is a fundamental right that is afforded protection by the Constitution and protection is afforded against interference by the State and interference by other persons.⁸ The enactment of retroactive taxation legislation poses a threat to the rule of law and the right to property as it may lead to legal uncertainty and result in arbitrary deprivation of property.

1.3 Purpose of the research

The concept of retroactive tax legislation needs to be critically analyzed in light of the fact that South Africa has a supreme Constitution that binds the legislature, the executive, the judiciary and all organs of state.⁹ The writer will discuss the rule of law and the effect of retroactive tax legislation on the rule of law as a value that is enshrined in the Constitution.¹⁰ This research will deal with the protection that is afforded to taxpayers from State interference with their property. In addition, the writer will discuss the effect of retroactive tax legislation on the right to property.

⁷ Eiselen, S & van Zyl, S.P. 2016. The retrospective amendments to tax legislation and the taxpayers right to property and Economic Freedom. *TSAR*, 3: 570.

⁸ Section 25(1) of the Constitution.

⁹ Section 2 and section 8 (1) of the Constitution.

¹⁰ Section 1 (c) of the Constitution.

The purpose is therefore to investigate whether retroactive tax legislation is in line with the Constitution. It is also the purpose of this study to analyze the manner in which Australia, the United Kingdom and the United States of America approach retroactive taxation legislation. These three foreign jurisdictions, like South Africa, are common law jurisdictions.¹¹ An investigation into how they deal with this concept is essential to determine if the practice in South Africa aligns with the practice in other countries.

1.4 Research Questions

The main research question is whether retroactive tax legislation passes the constitutionality muster. The sub-questions are firstly whether retroactive tax legislation accords with what is required by the rule of law, secondly whether retroactive tax legislation amounts to an arbitrary deprivation of property and if so whether such deprivation is justifiable. The last sub-question is how does Australia, the United Kingdom and the United States of America approach retroactive tax legislation.

1.5 Research objectives

The objectives of this research are:

- 1.5.1 To evaluate the relationship between the rule of law and the enactment of retroactive taxation legislation;
- 1.5.2 To investigate whether retroactive tax legislation amounts to a deprivation of property, if so, whether such deprivation is justifiable in an open and democratic society.
- 1.5.3 To determine if South Africa is dealing with this issue in a manner that is similar to how it is dealt with by foreign jurisdictions and whether there are different methods that South Africa may adopt from foreign jurisdictions.

¹¹ Brown, EF. 2010. A comparison of the handling of the financial crisis in the United States, the United Kingdom and Australia. *Villanova Law Review*, 55(3): 513.

1.6 Limitations and Assumptions

This research will be limited to a discussion of the rule of law, the right to property and the approach of foreign jurisdictions to retroactive tax law-making. The writer will rely on case law, textbooks, articles, legislation, dissertations and theses as authority for the submissions to be made. The writer will not make assumptions on points of law and facts.

1.7 Methodology

The writer will employ the constitutional analysis method to investigate the effect of retroactive tax legislation on the right to property, the rule of law and the manner in which foreign jurisdictions deal with retroactive tax legislation. This method should assist the writer in determining whether retroactive tax legislation is constitutional.

1.8 Chapter Exposition

Chapter 1 of this mini-dissertation deals with the background of the research, the problem statement and the purpose of the research.

Chapter 2 will provide a general overview of what the rule of law is and the relationship between the rule of law and retroactive tax legislation. This chapter will also deal with the principle of certainty and the role of the legislature and that of the judiciary in giving effect to the rule of law. This chapter is important because it will indicate, whether retroactive tax legislation conforms to the foundational values enshrined in the Constitution.

Chapter 3 will provide a discussion of what the right to property is and it will provide an analysis into whether the enactment of retroactive tax legislation amounts to an arbitrary deprivation of property. It will also discuss whether such deprivation, if any, is justifiable in an open and democratic society. This will assist in determining whether the enactment of retroactive tax legislation constitutes an unjustifiable infringement of the right to property and is therefore unconstitutional.

Chapter 4 will deal with the manner in which foreign jurisdictions deal with the concept of retroactive tax legislation. The writer will discuss the approach in Australia, the United Kingdom and the United States of America. The reason for selecting these three foreign jurisdictions is that they all have an attribute that is similar to South Africa which is that they are common law jurisdictions.¹²

Chapter 5 will be the conclusion of this research. It will provide a brief summary of the chapters that will have been dealt with. It will then attempt to provide an answer to the main research question.

¹² Brown, EF. 2010. A comparison of the handling of the financial crisis in the United States, the United Kingdom and Australia, 55(3):513.

Chapter 2: The rule of law

2.1 Introduction

The rule of law forms an essential part of South African law because the Constitution asserts it as a value on which the Republic of South Africa is founded.¹³ As the Constitution of the Republic of South Africa is supreme, the fact that the rule of law is a founding value of the Constitution indicates that the rule of law is very significant.¹⁴ Thus, it is important to consider the manner in which legislation or conduct that is brought under constitutional scrutiny relates to the fundamental values as enshrined in the Constitution, particularly the rule of law.

The rule of law is a value and not a right, therefore, one may not rely on it alone to pose a challenge on the constitutional validity of any law or conduct.¹⁵ The Constitutional court has held that the rule of law and other values in section 1 of the Constitution are essential as they inform and give meaning to the Constitution.¹⁶ In addition, the court stated that reliance should be placed on statute or on a specific right in the Constitution to challenge the conduct of an organ of state instead of a wide principle in the Constitution.¹⁷ However, the rule of law can be used as a yard stick to determine if a certain principle or conduct accords with the Constitution. The Constitutionality of retroactive taxation legislation has been brought under scrutiny in the matter of *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service*.¹⁸ This case has shed light on the need for a deeper investigation into the relationship between the rule of law and retroactive taxation legislation.

¹³ Section 1(c) of the Constitution.

¹⁴ Section 2 of the Constitution.

¹⁵ *Minister of Home Affairs v National Institute for Crime Prevention and the Re-Integration of Offenders (NICRO) and Others* 2005, at par 21.

¹⁶ *Minister of Home Affairs v National Institute for Crime Prevention and the Re-Integration of Offenders (NICRO) and Others*, at par 21.

¹⁷ Hoexter, C. 2007. *Administrative law in South Africa*, at p 226.

¹⁸ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service and Another* 2017 (6) SA 435 (GP).

This chapter will discuss the rule of law and the manner in which it relates to retroactive taxation legislation. Furthermore, this chapter will discuss the principle of certainty, the role of the legislature and the role of the judiciary in upholding the rule of law.

2.2 Background

The rule of law can be defined as an instrument that can be used by individuals to challenge government actions that disadvantage the individuals concerned.¹⁹ However, Richard and Fallon are of the view that defining the rule of law is a difficult exercise and they have argued that the exact meaning of the rule of law gets more difficult to discern with the passing of time.²⁰ The rule of law is also defined as procedural requirements that are bundled together and are aimed at achieving justice and fairness.²¹ It is important for those who are expected to act in accordance with the rule of law to understand what it is and what it requires of them. A clear and uniform definition is necessary to eliminate ambiguity, however its absence does not reduce the significance of the rule of law.

Devenish has captured the characteristics of the rule of law and they are said to include certainty, uniformity, impartiality and equity.²² These characteristics of the rule of law are an aspect that the legal scholars seem to agree on as they underlie all the proposed definitions of the rule of law that are mentioned in this chapter. Hoexter expressed the view that the rule of law is intended to ensure that the manner in which the government and individuals act is limited to the rules that were lawfully imposed on them.²³ Coetzer shares the same sentiments with Hoexter in this regard.²⁴ This definition of the rule of law is clear and comprehensive, most importantly, it highlights the fact that the rules

¹⁹ Costa, P. 2007. The rule of law: A historical introduction. In: Costa, P & Zolo, D. (eds) *The rule of law history, theory and criticism*. New York: Springer, 80: 74.

²⁰ Richard, H & Fallon, JR. 1997. The Rule of Law as a concept in a constitutional discourse. *Columbia Law Review*, 97: 1.

²¹ Sriram, C.L, Martin-Ortega, O & Herman J. 2011. Promoting the rule of law: from liberal to institutional peacebuilding. Sriram, C.L, Martin-Ortega, O & Herman J (eds). *Peacebuilding and the Rule of Law in Africa*. Oxon: Routledge, 3.

²² Devenish, G. 2004. The rule of law revisited with special reference to South Africa and Zimbabwe. *TSAR*: 675.

²³ Hoexter, C. 2007. *Administrative law in South Africa*. Cape Town at p226.

²⁴ Coetzer, N. 2017. More reflections on the rule of law. *Industrial Law Journal*, 38: 2217.

imposed by the government must be lawful. The test for lawfulness of rules will vary from one legal system to the next depending on the requirements for lawfulness of each legal system.

In light of the fact that the rule of law is a largely debated subject and that some legal scholars not only debate its characteristics but go as far as debating its very meaning, one has to look at the meaning that relates better to South African law. Of particular importance is to consider the rule of law as enshrined in the Constitution and the manner in which it is to be understood based in that context.

Henrico pointed out that in fact, the rule of law does not require a rigid definition for its purpose or its ability to function, and in addition, he stated further that the rule of law may mean different things to different people.²⁵ This is an interesting manner of dealing with the possible dilemma of the lack of definition of the rule of law, yet it can yield undesirable results if individuals and the government determine for themselves what the rule of law means. However, Henrico goes further to state that the “common-denominator” in fully appreciating the rule of law is that it seeks to ensure that people plan their affairs with confidence, certainty and with knowledge of what the law requires of them and that people are protected from arbitrary exercise of power by government officials.²⁶

2.3 Certainty

Certainty is essential in the law, in fact, its absence leads to confusion and many other undesirable and unintended outcomes. The rule of law requires that the law should be clear, be prospective instead of being retroactive and that the law should be easily accessible.²⁷ In essence, this re-enforces the requirement that the law must be specifically stated and one can deduce the reason for this requirement which is the protection of the interests of the people who need to align their actions with the law.

²⁵ Henrico, R. 2014. Re-visiting the rule of law and the principle of legality: judicial nuisance or licence? *TSAR*: 742.

²⁶ Henrico, R. 2014: 743.

²⁷ *President of the Republic of South Africa v Hugo* 1997 (4) SA 1 CC at par 99.

As highlighted above, it is desirable for the law to be prospective in nature rather than be retroactive.²⁸ This is particularly more desirable where legislation places an obligation on people to act in a certain manner and where it imposes consequences for failure to act in the required manner. This appears to be part of the considerations that led to the prohibition of the retroactive operation of legislation in criminal law in South Africa.²⁹ The Constitution prohibits conduct or legislation that will lead to the conviction of a person for conduct that was not a criminal offence at the time that it was committed.³⁰ The same rules do not apply in the civil context, no prohibition exists against retroactive civil legislation. However, there is a presumption against retroactivity in our law and according to that presumption, no statute will be construed to have retroactive application unless it is clear from the said statute that the intention of the legislature is to create retroactive application.³¹

A person must be able to ascertain what the law is to allow such person to conduct themselves in a manner that is in accordance with the law.³² It is undesirable for both natural and juristic persons to be left in a vulnerable position and for the government to exercise its authority over them in a manner that they cannot predict or try to avoid.

According to Dicey's explanation of the rule of law, certainty must be guaranteed by the courts through the enforcement of the rights of the taxpayers. In addition, the legislature should guarantee certainty by clearly and in advance stating what actions will be sanctioned and what actions will attract tax liability in the case of taxpayers.³³ It is worth noting that what is required in terms of the certainty principle is not the ability to predict with complete certainty what the outcome would be if a matter is taken to court for interpretation of the legislation. The rule of law prohibits legislation that changes the outcomes of actions that were concluded with reliance on the law that was in existence at the time that the actions were performed.

²⁸ Pagone, GT. 2009. Tax uncertainty. *Melbourne University Law Review*: 887.

²⁹ Section 35 (3) (l) of the Constitution.

³⁰ Section 35 (3) (l) of the Constitution.

³¹ *National Director of Public prosecutions v Carolus and others* 2000 (1) SA 1127 SCA at par 31.

³² *President of the Republic of South Africa v Hugo* 1997 (4) SA 1 (CC) at par 99.

³³ Popelier, P. 2000. Legal certainty and principles of proper law making. *European Journal of Law Reform*, 2: 327.

This in turn allows the people to have more confidence in the government and to be active participants in the economy without fear that in future their present actions may cause them financial prejudice. It is clear that the imposition of retroactive tax legislation does not align with the requirements of the certainty principle of the rule of law.

2.4 The legislature

The national legislative authority in South Africa is vested in parliament.³⁴ Parliament is charged with the general duty to pass legislation on any matter.³⁵ The Constitution does not expressly allow for the enactment of retroactive civil or tax legislation. However, the legislature appears to draw its powers to enact retroactive tax legislation from the general legislative powers granted to it by the Constitution. From the definition of retroactive fiscal legislation that has been provided above, it appears that the enactment of retroactive taxation legislation may have adverse implications on taxpayers. This is because a change in the consequences of a past action means that taxpayers cannot change their actions to conform to the law.

Certainty is one of the important incidents of the rule of law and it has been held to be the very “manifestation” of the rule of law.³⁶ It is on this premise that there seems to be a clash between the requirements of the rule of law and the conduct of imposing legislation that has retroactive effect by the legislature.

The rule of law must be a thread that runs through all legislation that is enacted by the legislature. Moreover, legislation that is prospective in nature is ideal as the individuals are given the opportunity to perform actions with a full appreciation of the outcomes of their actions. The legislature should therefore ensure that legislation that is passed does not violate the principles as contained in the Constitution which include the rule of law and legal certainty.

³⁴ Section 43(a) of the Constitution.

³⁵ Section 44(1) (a) of the Constitution.

³⁶ Moyo, A. 2009. Defending human rights and the rule of law by the SADC Tribunal: *Campel* and beyond. *African Human Rights Law Journal*: 611.

2.5 The role of the judiciary

Judicial impartiality is an incident of the rule of law that has the traits of both English and Roman law.³⁷ The judiciary has a significant role in a constitutional dispensation, in fact, the judiciary is the guardian of the Constitution in South Africa. The courts are vested with the power to make a declaration of invalidity against all conduct or legislation that is in conflict with the Constitution.³⁸ This means that even if legislation that is unconstitutional is passed by the legislature, such legislation will be declared invalid once it is brought before the judiciary. Such safe guard, in an ideal world, would ensure that legislation that does not pass the constitutionality muster does not prevail.

The courts have a duty to ensure that the manner in which other organs of state exercise their power falls within the parameters of the Constitution, this is an ongoing duty that must be exercised diligently.³⁹ The judiciary should therefore safe guard the interests of the individuals, taxpayers in this instance, who may otherwise be prejudiced by the actions of organs of state. The *Pienaar Brothers v Commissioner for the South African Revenue Service* case forms part of the instances where the judiciary could have made a ruling that leads to the protection of the taxpayers, however that opportunity was missed.⁴⁰

In this case Pienaar Brothers (Pty) Ltd sought an order, among others, declaring that section 34(2) of the Taxation Laws Amendment 8 of 2007 which amended the Income Tax Act 58 of 1962 was unconstitutional.⁴¹ Pienaar Brothers sought a declaration of invalidity of section 34(2) insofar as it provided for the retroactive application of section 44(9A) of the Income Tax Act, which was introduced by Section 34(1)(c) of the Taxation Law Amendment Act.⁴² The Court held that although certainty is an important principle of law, the legislature should be able to change laws.⁴³ This finding by the court seems

³⁷ Devenish, G. 2004. The rule of law revisited with special reference to South Africa and Zimbabwe. TSAR: 675.

³⁸ Section 172(1) of the Constitution.

³⁹ Powell, C. 2017. Law as justification: Glenister, separation of powers and the rule of law. *Acta Juridica*.

⁴⁰ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service and Another*.

⁴¹ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service*, at par 1.

⁴² *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service* at par 1.

⁴³ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service* at par 46.

to not fully portray the significance of the rule of law especially certainty, which is a characteristic of the rule of law.

According to Tredoux and van Zyl the manner in which the court dealt with the issue of retroactivity in the *Pienaar Brothers* case is unsatisfactory as the court did not take into account the taxpayer's right to property in relation to the right to tax certainty.⁴⁴ The right to tax certainty is not specifically mentioned in the Constitution or legislation in South Africa, therefore it seems that the two authors are referring to certainty as a requirement of the rule of law. This view of Tredoux and van Zyl correctly encapsulates the manner in which the *Pienaar Brothers* case was dealt with by the judiciary. While it is true that the legislature is allowed to change laws, such changes should not unjustifiably interfere with the rights of the taxpayers. Furthermore, the changes to legislation should not be contrary to principles and values that are clearly stated in the Constitution.

Botha and Marupen agree with the judgment in the *Pienaar Brothers* case and their argument is that adequate notice of the proposed tax change was given to Pienaar brothers and other taxpayers.⁴⁵ They are of the view that because adequate notice was given then the challenged retroactive amendment of the Income Tax Act is not unconstitutional.⁴⁶ However, the court expressly stated that not even 'adequate' notice is necessary instead, the fact that there was notice that legislation would be introduced with retrospective effect in future was sufficient according to the court.⁴⁷ Camay holds a different view from that of Botha and Marupen, she states that the introduction of legislation retroactively which was confirmed as being constitutional in the *Pienaar brothers* case is in conflict with the principle of certainty.⁴⁸

The judiciary is vested with the power to intervene, upon being called to do so and make declarations of invalidity where appropriate. However, that does not seem to be

⁴⁴ Tredoux, LG & van Zyl, SP. 2018. Some Drastic Measures to Close a Loophole: The Case of *Pienaar Brothers (PTY) LTD v Commissioner for the South African Revenue Service* (87760/2014) [2017] ZAGPPHC 231 (29 May 2017) and the Targeted Retroactive Amendment of Section 44 of the *Income Tax Act* 58 of 1962

⁴⁵ Botha, H & Marupen, C.2017. Retrospective legislation: The *Pienaar Brothers* case. *Siber Ink*, 19.

⁴⁶ Botha, H & Marupen, C.2017. Retrospective legislation: The *Pienaar Brothers* case. *Siber Ink*, 19.

⁴⁷ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service* at par 85.

⁴⁸ Camay, A. 2017. The perils of introducing tax legislation by press release. *SA Financial Regulation Journal* [ONLINE] Available from: <http://financialregulationjournal.co.za/2017/10/18/the-perils-of-introducing-tax-legislation-by-press-release/> [Accessed on 17-11-2018].

happening as the legislature is still allowed to legislate retroactively in the tax law sphere. Even when the *Pienaar Brothers* matter, which highlighted a problematic practice, was brought before the court, the court elected not to act decisively in the interest of upholding the Constitution. The role of the judiciary is not a passive one but is a role that requires active steps towards the protection of individuals from the exercise of power by the state that has a detrimental effect on the individuals.

2.6 Conclusion

The rule of law is an essential value that underlies the Constitution and it should be taken into consideration when determining whether legislation or conduct is in line with the Constitution.⁴⁹ Furthermore, legal certainty as a characteristic of the rule of law has been discussed in this chapter and this chapter has shown that the imposition of retroactive tax legislation offends the principle of legal certainty. The reason for this assertion is that retroactive tax legislation deprives individual taxpayers of the opportunity to predict the outcomes of their conduct and plan accordingly.

The legislature has the authority to enact legislation however such authority must be exercised in a manner that conforms to the Constitution. The judiciary is there as a last resort for the individuals who are aggrieved by the conduct of organs of state and it possesses the power to intervene when organs of state act in a manner that is contrary to the Constitution. However, it appears that the enactment of retroactive taxation legislation is currently not an issue that is considered by the judiciary to be a violation of the rule of law.

⁴⁹ Section 1(c) of the Constitution.

Chapter 3: The right to property

3.1 Introduction

Prior to 1994 parliament was supreme in South Africa and laws that were enacted by parliament could not be invalidated by the courts.⁵⁰ This meant that all laws, regardless of whether they were unjustifiable or unreasonable, had to be enforced. The legitimacy of the enacted laws could not be challenged as there was no supreme Constitution against which legislation could be tested. The right to property prior to 1994 was enforced through reliance on common law which was Roman- Dutch law.⁵¹ In effect the protection or enforcement of the right to property was not primarily drawn from legislation.

There was a change in our law in 1994 when the Interim Constitution came into effect. The right to property was deemed worthy to be enshrined in the Interim Constitution.⁵² Subsequent to its inclusion in the Interim Constitution it was then incorporated in the final Constitution of the Republic of South Africa.⁵³ The right to property is contained in the Bill of rights which form chapter 2 of the Constitution. It is a fundamental human right that is enshrined in the Constitution. The right to property includes a taxpayer's right to be protected from State interference with the taxpayer's property.⁵⁴ Instead of parliamentary sovereignty, South Africa has a supreme Constitution which mandates that law and conduct that is not consistent with it must be declared invalid.⁵⁵ It follows that when enacting legislation, parliament must align such legislation with the supreme law of the land.

Legislation that relates to the collection of revenue has a significant role in the proper functioning of the country, however such legislation is not above the Constitution and it

⁵⁰ Croome, B. 2002. Constitutional law and taxpayer's rights in South Africa. *Acta Juridica*, 1.

⁵¹ Lewis, C. 1992. The right to private property in a new political dispensation in South Africa. *South African Journal on Human Rights*: 393.

⁵² Section 28 of the Interim Constitution of the Republic of South Africa, Act 200 of 1993.

⁵³ Section 25 of the Constitution, 1996.

⁵⁴ Section 25 of the Constitution, 1996.

⁵⁵ Section 2 of the Constitution, 1996.

must be aligned with the Constitution.⁵⁶ Therefore, in a constitutionality enquiry, fiscal legislation stands at an equal footing with any other legislation and has to conform to the norms and standards that are set by the Constitution. This chapter provides a discussion of the right to property as enshrined in the Constitution. Furthermore, this chapter will examine the relationship between the right to property and the enactment of taxation legislation with retroactive effect. This research will also analyse the manner in which the conflicting interests between those of the taxpayers and the state can be balanced. Lastly, this chapter will provide a discussion of the limitation clause in the Constitution and will also discuss the relevance of this section when dealing with the right to property.

3.1.1 The right to property explained

The right to property is a fundamental right that is protected in terms of section 25 of the Constitution. No uniform definition of property has been developed yet by either the courts, the legislature or the academics. The Constitution also does not provide a definition of the property that is protected under section 25. The closest that section 25 gets to shedding light on the meaning of property is the statement in section 25(4) (b) to the effect that property is not limited to land. According to Currie and de Waal there are a number of different meanings that can be ascribed to property and it is a concept that is almost impossible to define with absolute precision.⁵⁷

In *Shoprite Checkers (Pty) Ltd v MEC for Economic Development* the Applicant approached the Constitutional Court for a confirmatory order. The Eastern Cape Division had made a declaration of invalidity against some provisions of the Eastern Cape Liquor Act and the Applicant approached the Constitutional Court to confirm that order of invalidity.⁵⁸ The Constitutional court expressed concern about the lack of common ground on how property is perceived and that this may pose a threat to the

⁵⁶ *First National Bank of SA LTD t/a Wesbank v Commissioner, South African Revenue Service and another; First National Bank of SA LTD t/a Wesbank v Minister of Finance* at par 31.

⁵⁷ Currie, I & de Waal, J.2016. *The bill of rights handbook* at p 535.

⁵⁸ *Shoprite Checkers (Pty) Ltd v MEC for Economic Development, Environmental affairs and Tourism* at par 2.

South African constitutional dispensation.⁵⁹ Having made this statement, the court did not attempt to provide a definition for property in order to remedy the identified problem area. The Constitutional Court then held that grocer's wine licenses constitute property under section 25 of the Constitution thereby indicating that the enquiry into whether an interest is property will be dealt with on its own merits.⁶⁰

In the *First National Bank* case the Constitutional Court held that it would be judicially unwise to even attempt to give an all-inclusive definition of property considering the level of the South African constitutional jurisprudence.⁶¹ This view of the court allows for flexibility in the law as it means that the courts can properly apply their discretion instead of being limited by a rigid definition. However, this approach is flawed because it perpetuates uncertainty in the law which is not a desirable result for taxpayers. Badenhorst expressed the view that an interest or a right should be regarded as property in the constitutional context if it is a concrete asset that has been acquired by the holder under normal law.⁶² However, according to Croome a taxpayer's entitlement to certain benefits or rights constitutes property in the constitutional context.⁶³ The view expressed by Croome is more preferable in that it takes into account the evolving nature of property and does not only limit it to tangible assets.⁶⁴

The absence of a comprehensive definition for property is an issue that the litigants have to struggle through and one that either the judiciary or the legislature have to address. Solace can be found in the knowledge that the judiciary will deal with a contention that a certain interest constitutes constitutional property on a case by case basis. In light of the above, especially the views expressed by Croome and the court in the *Shoprite* case, money belonging to the taxpayer will constitute property that is worth

⁵⁹ *Shoprite Checkers (Pty) Ltd v MEC for Economic Development, Environmental affairs and Tourism* at par 4.

⁶⁰ *Shoprite Checkers (Pty) Ltd v MEC for Economic Development, Environmental affairs and Tourism*) at par 5.

⁶¹ *First National Bank of SA LTD t/a Wesbank v Commissioner, South African Revenue Service* at par 51.

⁶² Badenhorst P.J. 2017. The Notion of Constitutional Property in South Africa: An analysis of the Constitutional Court's approach in *Shoprite Checkers (Pty) Ltd v MEC for Economic Development, Eastern Cape* 2015 (6) SA 125 (CC) *Stell LR*: 29.

⁶³ Croome, B. 2010. *The taxpayer's rights in South Africa* at p 18.

⁶⁴ Although Croome makes reference to a taxpayer, the view expressed is not limited to taxpayers, it is flexible enough to accommodate a variety of persons.

protection. This is based on the entitlement that the taxpayer has on the money and other rights that attach to such entitlement.

3.1.2 Deprivation of property

The Constitution provides that;

“No one may be deprived of property except in terms of the law of general application and no law may permit arbitrary deprivation of property.⁶⁵”

The Constitution only allows deprivation of property if it is in terms of the law of general application. Ordinarily, retroactive fiscal legislation is drafted in a manner that makes it applicable generally and it would thus be permitted if found to be a deprivation in so far as it is not arbitrary. Whether a person has been deprived of property will depend on the extent of the interference with the rights to the property that is afforded protection by the Constitution.⁶⁶ This statement expresses the view that not all interference by the State with the property of the taxpayer will amount to a deprivation of property. For example, legislation that requires a taxpayer to pay tax upon conclusion of a certain act will have a lesser probability of constituting a deprivation of property where it is made to operate from present to the future. However, where fiscal legislation is imposed with retroactive effect and has the effect of creating financial obligations for the taxpayer, such legislation leads to a deprivation of property as the extent of the interference is major. This is also because the taxpayer is obliged to comply with the legislation while it is in effect. It appears from what has been stated above that deprivation of property amounts to a limitation or complete confiscation of the taxpayer’s rights to the taxpayer’s property.

According to Croome, the payment of tax constitutes a deprivation of property because payment of tax is not optional but is mandated by the law.⁶⁷ In addition thereto, there are penalties that may be imposed should a taxpayer fail to effect payment of tax. The payment of tax as a result of a retroactive fiscal provision would therefore be a clearer

⁶⁵ Section 25 of the Constitution, 1996.

⁶⁶ *National Credit Regulator v Opperman and Others* 2013 (2) SA 1 (CC) at par 66.

⁶⁷ Croome, B. 2010. *The taxpayer’s rights in South Africa*, at par p 19.

deprivation of property as the taxpayer would have to pay tax that was not even payable at the time when a certain transaction was entered into. Croome goes further and argues that the introduction of taxation legislation with retroactive effect amounts to a deprivation of property because it leads to the seizure of the property to which the taxpayer is entitled based on legislation that was not in operation when the past even happened.⁶⁸

Furthermore, the Tax Administration Act provides that an obligation to pay tax and the right of SARS to receive payment of tax will not be suspended as a result of an objection by the taxpayer to payment.⁶⁹ Therefore, the taxpayers cannot retain their property whilst challenging retroactive fiscal laws. In addition, failure to comply with tax Acts is a criminal offence in terms of the Tax Administration Act.⁷⁰ The taxpayers are therefore compelled by legislation to comply with fiscal legislation regardless of whether it is operating prospectively or retroactively. This further supports the contention that retroactive fiscal legislation amounts to a deprivation of property.

3.1.3 Arbitrary deprivation of property

The government determines the methods and levels of taxation based on the economic growth, the rate of inflation and shortfall in the budget.⁷¹ The measures undertaken by the government to collect revenue, which are mostly in the form of legislation, are subject to the Constitution which is the supreme law of the land.⁷² The Constitution prohibits arbitrary deprivation of property therefore, once it has been established that legislation constitutes a deprivation of property, the next step is to determine if the legislation is arbitrary in nature.⁷³ The meaning of 'arbitrary' like other terms that are contained in section 25 of the Constitution is not defined in the Constitution. Reliance is therefore placed on the legal scholars and ultimately the courts to give meaning to this concept.

⁶⁸ Croome, B. 2010. *The taxpayer's rights in South Africa*, at p 63.

⁶⁹ Section 164(1) of the Tax Administration Act 28 of 2011.

⁷⁰ Section 234 and 235 of the Tax Administration Act.

⁷¹ Croome, B. 2010. *The taxpayer's rights in South Africa*, at p 2.

⁷² Section 2 of the Constitution.

⁷³ Section 25(1) of the Constitution.

In determining whether the deprivation of property is arbitrary, a balance must be struck between the protection of existing property interests and the promotion of public interests which flow from the objectives of developing the society we live in.⁷⁴ According to Currie and de Waal, a deprivation of property will be arbitrary if it is procedurally and substantively unfair.⁷⁵ Where legislation has the effect of depriving a person of their property, the proper procedure must be followed.

In the *First National bank* case FNB approached the Constitutional Court directly in an appeal against the decision of the Cape of Good Hope High Court which dismissed their constitutional challenge of section 114 of the Customs and Excise Act 91 of 1964.⁷⁶ The court held that a deprivation of property will be arbitrary where there are insufficient reasons for it.⁷⁷ The court then provided factors to be considered in determining whether legislation amounts to an arbitrary deprivation of property. Such factors include the following:

“(a) It is to be determined by evaluating the relationship between means employed, namely the deprivation in question and ends sought to be achieved, namely the purpose of the law in question.

(b) A complexity of relationships has to be considered.

(c) In evaluating the deprivation in question, regard must be had to the relationship between the purpose for the deprivation and the person whose property is affected.

(d) In addition, regard must be had to the relationship between the purpose of the deprivation and the nature of the property as well as the extent of the deprivation in respect of such property.

(e) Generally speaking, where the property in question is ownership of land or a corporeal moveable, a more compelling purpose will have to be established in order for the depriving law

⁷⁴ *Shoprite Checkers (Pty) Ltd v MEC for Economic Development, Environmental affairs and Tourism*.

⁷⁵ Currie, I. & de Waal, J. 2016. *The Bill of Rights Handbook*, at p 540.

⁷⁶ *First National Bank of SA LTD t/a Wesbank v Commissioner, South African Revenue Service* at par 1.

⁷⁷ *First National Bank of SA LTD t/a Wesbank v Commissioner, South African Revenue Service* at par 1.

to constitute sufficient reason for the deprivation than in the case when the property is something different and the property right something less extensive.”⁷⁸

The court held that when the deprivation in question affects all the aspects of ownership then the purpose for the deprivation must be more persuasive than in cases where only part of the ownership rights are affected.⁷⁹ In essence, this means that where the taxpayer loses all ownership rights as a result of the deprivation then such deprivation has a high prospect of being an arbitrary deprivation of property. On the other hand if the deprivation only affects a minor part of the taxpayer’s ownership property rights, an example is where a deprivation amounts to a provisional suspension of the taxpayer’s right to use its property, then such deprivation has a lower prospect of being arbitrary. Furthermore, the court held that in other cases the fact that a statute is rationally linked to the purpose for which it was enacted, will not suffice to justify a deprivation, instead the deprivation may only be justifiable in terms of 36(1) of the Constitution.⁸⁰ Lastly the court stated that when deciding whether a deprivation of property is arbitrary, the court must consider the facts of each particular case.⁸¹

The relationship between the state and the individual taxpayer is a complex one because the state is at a position of power in comparison to the taxpayer. The state has mechanisms in place to enforce payment of tax such as the imposition of penalties and may also include the institution of legal proceedings against taxpayers. On the other hand, the taxpayer does not have powers over the state and that is the reason why taxpayers need protection from the exercise of power by the government. Although, the taxpayer has the duty to pay tax and such duty flows from legislation, it would not be fitting to place the burden on taxpayers retroactively. This is because the taxpayers then have no way of avoiding or minimizing such a burden. Furthermore, the deprivation that

⁷⁸ *First National Bank of SA LTD t/a Wesbank v Commissioner, South African Revenue Service* at par 100.

⁷⁹ *First National Bank of SA LTD t/a Wesbank v Commissioner, South African Revenue Service* at par 100.

⁸⁰ *First National Bank of SA LTD t/a Wesbank v Commissioner, South African Revenue Service* at par 100.

⁸¹ *First National Bank of SA LTD t/a Wesbank v Commissioner, South African Revenue Service* at par 100.

results from retroactive fiscal legislation is one that embraces all aspects of property as the taxpayer is permanently deprived of its property in the form of money.⁸²

Procedural fairness means that the state must base the exercise of its power on rules that are plainly set out.⁸³ The courts must therefore conduct a balancing enquiry when determining whether legislation constitutes arbitrary deprivation of property. In determining whether a rule is substantively arbitrary the reason for the deprivation must be established and the reasons provided must be sufficiently linked to the purpose that is sought to be achieved.⁸⁴

In *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service* the Applicant had entered into an amalgamation transaction with the aim to introduce a BEE component in the company.⁸⁵ After completion of the transaction, the directors of the Applicant decided to issue a distribution amounting to R29 000 to the shareholders from the share premium account.⁸⁶ At the time when the distribution was made, it did not constitute a dividend in terms of the Income Tax Act and the distribution was implemented on 3 May 2007.⁸⁷ On 8 August 2007 the Taxation Laws Amendment Act 8 of 2007 was promulgated.⁸⁸ The promulgation of the Taxation Laws Amendment Act took place about two months after the distribution was finalized. The effect of this Act was that it introduced Secondary Tax on Companies in respect of shares that were issued from the share premium account and provided for retroactive application of this new provision.

The Applicant then found itself in a position where it had to effect payment of tax that was not applicable at the time when it concluded the redistribution agreement. The court was approached to remedy the situation by declaring section 34(2) unconstitutional on

⁸² Croome, B. 2010. *The taxpayer's rights in South Africa*, at p 63.

⁸³ Currie, I. & de Waal, J. 2016. *The Bill of Rights Handbook*, at p 541.

⁸⁴ *First National Bank of SA LTD t/a Wesbank v Commissioner, South African Revenue Service* at par 100.

⁸⁵ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service* at par 3.

⁸⁶ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service* at par 11.

⁸⁷ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service* at par 11.

⁸⁸ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service* at par 11.

the basis that it amounts to an infringement of the Applicant's rights in terms of section 25 of the Constitution in so far as it creates a retroactive liability to pay tax.⁸⁹

In determining whether legislation constitutes an arbitrary deprivation the means employed must be evaluated against the ends sought to be achieved.⁹⁰ The court must therefore consider whether the action of the state bears relation to the purpose that the state wants to fulfill. The main purpose of taxation is to enable the government to collect revenue and such revenue is then spent by the state on goods and services that are deemed a necessary expenditure for the state. The purpose of the legislation imposed is legitimate in so far as it is aimed at the collection of revenue for the benefit of the country. The issue is that there seems to be no correlation between the ends sought to be achieved and the means employed in that a similar objective would have been achieved had the statute been made to operate prospectively.

The Court held that the State used a recognised mechanism to close the loophole and that the state did not specifically target the Applicant.⁹¹ The loophole that the court was referring to was the exclusion of the amounts paid from a share premium account from the definition of 'dividend' in the Income Tax Act. This decision of the High Court seems to favour the view that retroactive fiscal legislation is acceptable and recognised as constitutionally valid. The court held that the retroactive amendment of the Income Tax Act was not arbitrary and consequently, no order of constitutional invalidity could be made. In determining whether the amendment constituted arbitrary deprivation of property, the court seemingly did not consider balancing the conflicting interests as stated in the *First National Bank* case.⁹² The enquiry into arbitrariness should not be one sided as that would yield undesirable results.

Tredoux and van Zyl argue that legislation may not be affected retroactively with the aim to collect revenue lost revenue.⁹³ Furthermore, they argue that retroactive fiscal

⁸⁹ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service* at par 1.

⁹⁰ *First National Bank of SA LTD t/a Wesbank v Commissioner, South African Revenue Service* at par 100.

⁹¹ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service* at par 110.

⁹² *First National Bank of SA LTD t/a Wesbank v Commissioner, South African Revenue Service* at par 100.

⁹³ Tredoux, LG & van Zyl, SP. 2018. Some Drastic Measures to Close a Loophole: The Case of *Pienaar Brothers (PTY) LTD v Commissioner for the South African Revenue Service* (87760/2014) [2017]

legislation may not be made to operate retroactively to affect completed transactions.⁹⁴ The *Pienaar brothers* case involved a retroactive statute that was aimed at both recovering lost revenue and it affected a completed transaction. Tredoux and van Zyl express the view that the conclusion by the court that the retroactive legislation was rational and thus constitutional in the *Pienaar Brothers* case was incorrect.⁹⁵ This view is in line with the findings of this research, this is based on the fact that so far this study has shown that the decision in *Pienaar brothers* does not correctly reflect the enquiry into the constitutionality of a statute. It is for that reason that a proper and correct conclusion could not be reached by the court in the *Pienaar Brothers* matter.

According to Kruger, a constitutional challenge on taxation with a retroactive effect must be based on the principle of legality which requires that all government conduct must be rational.⁹⁶ Kruger further states that a challenge in the manner that he proposes is not likely to succeed as it is a low threshold and the courts are more likely to find in favour of the government.⁹⁷ There is no need to rely on an implied or even express value of the Constitution when the taxpayer can rely on an expressly stated right in the Constitution to challenge retroactive tax legislation. The approaches that are adopted by Tredoux and van Zyl and Kruger are both offer a solution to the difficulty posed by retroactive taxation legislation, although the proposed solutions differ.

It appears that the court in *Pienaar Brothers*⁹⁸ did not properly apply the principles laid down in *First National Bank* when deciding on the constitutionality of retroactive fiscal

ZAGPPHC 231 (29 May 2017) and the Targeted Retroactive Amendment of Section 44 of the *Income Tax Act 58 of 1962*, at par 26.

⁹⁴ Tredoux, LG & van Zyl, SP. 2018. Some Drastic Measures to Close a Loophole: The Case of *Pienaar Brothers (PTY) LTD v Commissioner for the South African Revenue Service* (87760/2014) [2017] ZAGPPHC 231 (29 May 2017) and the Targeted Retroactive Amendment of Section 44 of the *Income Tax Act 58 of 1962*, at par 26.

⁹⁵ Tredoux, LG & van Zyl, SP. 2018. Some Drastic Measures to Close a Loophole: The Case of *Pienaar Brothers (PTY) LTD v Commissioner for the South African Revenue Service* (87760/2014) [2017] ZAGPPHC 231 (29 May 2017) and the Targeted Retroactive Amendment of Section 44 of the *Income Tax Act 58 of 1962*, at par 26.

⁹⁶ Kruger, L. 2014. Retrospective legislation: Do taxpayers have any recourse? *Business Tax & Company Law Quartely*, 5 (1): 19.

⁹⁷ Kruger, L. 2014. Retrospective legislation: Do taxpayers have any recourse? *Business Tax & Company Law Quartely*, 5 (1): 20.

⁹⁸ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service*.

legislation. The court in *Pienaar Brothers*⁹⁹ had an opportunity to exercise its judicial functions and protect the property rights of the taxpayers that are guaranteed by section 25 of the Constitution. The effect of this decision is that retroactive fiscal legislation remains permissible in South Africa. It has been shown above that the enactment of retroactive taxation legislation amounts to an arbitrary deprivation of property. This finding is sufficient for a court to make a declaration of invalidity against such retroactive tax legislation.

3.2 The limitations clause

Section 36 of the Constitution provides that the rights in the Bill of Rights may be limited only in terms of law of general application. This section further provides that such limitation must be reasonable and justifiable in an open and democratic society.¹⁰⁰ This means that even if legislation is found to be arbitrary in terms of Section 25 of the Constitution, Section 36 will have to be applied to determine if the limitation of the right can be justified in terms of Section 36. The application of section 36 is also necessary because section 36 is more detailed and it even provides factors that must be considered to determine whether a limitation is reasonable and justifiable.

According to *Cheadle et al*, where it has been found that legislation or conduct amounts to an arbitrary deprivation of property then the courts must declare such legislation unconstitutional without considering section 36 of the Constitution.¹⁰¹ The reason for this contention is that an arbitrary deprivation of property can never be “reasonable and justifiable in an open and democratic society based on human dignity, equality and freedom.”¹⁰² This contention is persuasive because section 36 of the Constitution provides that “the rights in the Bill of Rights may be limited”... it would appear that the right to property also falls into this category and therefore the provisions of section 36 should be taken into account.

⁹⁹ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service*.

¹⁰⁰ Section 36 of the Constitution.

¹⁰¹ Cheadle, MH & Davis, DM & Haysom, NRL. 2002. *South African Constitutional law: The Bill of rights*, at p 462.

¹⁰² Cheadle, MH & Davis, DM & Haysom, NRL. 2002. *South African Constitutional law: The Bill of rights*, at p 462.

Section 25 (1) also provides for the need for law of general application where there is a deprivation of property, this means that if a deprivation of property is not effected through law of general application then it will fail the test of constitutionality. In this regard, section 25(1) and 36 would yield similar results. As stated above, section 36 is more detailed and it provides that all relevant factors must be taken into account in determining whether the limitation of a right in the Bill of Rights is reasonable and justified. Furthermore, section 36 provides a list of factors to be taken into account in such an enquiry.

The factors that are stated in section 36 include the relation between the limitation and its purpose, the importance of the limitation and whether there are less restrictive means to achieve the purpose.¹⁰³ A balance must be struck between retroactive fiscal legislation and the rights of the taxpayer. In *Shoprite Checkers v MEC for Economic Development* the court held that where there are less invasive measures that can be employed by the legislature then such measures should be employed.¹⁰⁴ The court was re-enforcing one of the factors stated in section 36 of the constitution. According to Croome the specific reference to “less restrictive measures in the Constitution is significant and taking from this principle, it is clear that the preferable situation is for legislation to be prospective.¹⁰⁵ It is therefore, not sufficient for the legislature to impose legislation that attaches new consequences to past actions only on reason that doing so will lead to the collection of more revenue by the fiscus. It is specifically unacceptable where there are less restrictive measures that can be employed. Tredoux and van Zyl point out that in the *Pienaar Brothers* case there were alternative measures that could have been utilised by the state and the failure to employ such measures further indicates the unconstitutionality of the retroactive legislation.¹⁰⁶

3.3 Conclusion

¹⁰³ Section 36 (1) of the Constitution.

¹⁰⁴ *Shoprite Checkers (Pty) Ltd v MEC for Economic Development, Environmental affairs and Tourism*.

¹⁰⁵ Croome, B. 2010. *The taxpayer's rights in South Africa*, at p65.

¹⁰⁶ Tredoux, LG & van Zyl, SP. 2018. Some Drastic Measures to Close a Loophole: The Case of *Pienaar Brothers (PTY) LTD v Commissioner for the South African Revenue Service* (87760/2014) [2017] ZAGPPHC 231 (29 May 2017) and the Targeted Retroactive Amendment of Section 44 of the Income Tax Act 58 of 1962, at par 26.

The right to property has been discussed in this chapter and it has been shown that legal scholars and courts have provided guidance with regards to a proper interpretation of what constitutes property in the constitutional sense. This chapter has also shown that the enactment of retroactive fiscal legislation amounts to an interference with the property of the taxpayers which property is in the form of money. Moreover, this chapter has detailed how the retroactive tax legislation amounts to an arbitrary deprivation of property. Of specific importance is the fact that this chapter has highlighted that the *FNB* case has laid down principles and factors to be used in determining the constitutionality of a fiscal statute or conduct. The court's ruling in the *Pienaar Brothers*¹⁰⁷ case could have set a precedent that leads to the protection of the rights of the taxpayers, however the court decided against this. In addition, the court in the *Pienaar Brothers*¹⁰⁸ case neglected to use the mechanism that was set in motion in the *FNB* case in order to reach a proper decision. The legislature has the option of enacting legislation that operates prospectively to ensure that the existing rights of the taxpayers are not destabilized instead of enacting retroactive legislation that has adverse financial consequences for the taxpayers.

¹⁰⁷ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service.*

¹⁰⁸ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service.*

CHAPTER 4: Foreign law

4.1 Introduction

South Africa is a relatively young constitutional dispensation, as such it is essential to take cognisance of the legal approaches of other countries. The purpose of this is to determine if there are progressive methods that South Africa can adopt from other countries which could be used to enhance our legal system. The Constitution of the Republic of South Africa supports this view by stating that the courts may consider foreign law when interpreting the Bill of Rights.¹⁰⁹

Unlike international law which the courts are obliged to consider, the consideration of foreign law is left to the discretion of the courts.¹¹⁰ Although this means that foreign law is not binding on the South African courts, it does not mean that it is insignificant. On the contrary, foreign law carries persuasive weight in the South African courts. An enquiry into the constitutionality of retroactive tax legislation is determined with reference to the Constitution of South Africa, foreign law is not a decisive factor in such an enquiry but it is significant for the reasons that have been stated above.

This chapter briefly explores the manner in which foreign jurisdictions deal with the concept of retroactive taxation legislation. The United Kingdom, the United States of America and Australia are all countries that apply the common law. There are a number of common law jurisdictions in the world, discussing all of them would be time consuming and impractical for purposes of this research. It is for that reason that only the three countries that are mentioned above will be considered in this paper. The position in the United Kingdom and in USA was considered by the court in the *Pienaar Brothers* case and this was done very briefly. Therefore these two countries are discussed to get a view of their legal systems that is more in depth than the one provided in the *Pienaar Brothers* case. A discussion of the Australian legal system is included because Australia is also a constitutional country. This chapter will first discuss

¹⁰⁹ Section 39 of the Constitution.

¹¹⁰ Section 39 of the Constitution.

the position in the United States of America, followed by a discussion of the position in the United Kingdom and subsequently, Australia.

4.2 United States of America

The United States of America is similar to South Africa in that both countries have supreme Constitutions. Because of the similarities between the South African and the USA legal system which include the application of the common law and the supremacy of their Constitutions, these two countries are comparable for purposes of this dissertation. The aim of the comparison is to obtain guidance on how to deal with retroactive taxation statutes. The fact that these two jurisdictions are common law jurisdictions means, among other things, that both these countries adhere to the principle of the hierarchy of the courts and the independence of the judiciary.¹¹¹ It would therefore be less cumbersome to import the methods applied in the USA to South Africa compared to a country that has less similarities with the South African legal system. This would be done to deal with the concept of retroactive fiscal legislation, should such approaches offer viable guidance to South Africa.

In terms of the Constitution of the USA, the enactment of law with retroactive effect is prohibited only in criminal matters and penal laws in the USA.¹¹² However, revenue law is not regarded as penal law in the USA.¹¹³ This feature of the USA Constitution is similar to section 35 (3)(l) of the South African Constitution which provides that an accused person may not be convicted for an act that was not an offence at the time when such act was committed.

The Constitution of the United States provides that the State and the United States may not take private property from individuals without following due process of the law.¹¹⁴

¹¹¹ Koonar, S. 2010. Justice systems in Canada and the United States.[ONLINE] Available from: https://www.americanbar.org/content/newsletter/publications/law_trends_news_practice_area_e_newsletter_home/10_summer_lit_feat1.html [Accessed on 2-10-2018].

¹¹² This is in terms of Article I, section 9, clause 3 of the Constitution of the United States of America.

¹¹³ Neuhoff, RR. 1935. Retrospective Tax Laws at p 1.

¹¹⁴ Neuhoff, RR. 1935. Retrospective Tax Laws at p 2; the Constitution of the USA Amendment 5.

Therefore the test to determine whether a retroactive fiscal statute is constitutional is whether such statute is in accordance with due process of the law. In *PBGC v. R. A. Gray & Co.*, the U.S Supreme Court had to decide on whether the enacted retroactive legislation was in conflict with the due process requirement of the Constitution and thus invalid.¹¹⁵ Congress had passed a statute which created a government owned entity, which in turn, provided insurance to private pension funds where the pension plan terminated while there were insufficient assets for the guaranteed benefit.¹¹⁶ It then became apparent to Congress that a large number of pension plans were facing financial difficulty which would lead to a large number of terminations and would place a burden that it too strenuous on the government entity that was created.¹¹⁷ Congress then enacted another Act which required employers who were withdrawing from a pension plan to pay a fixed amount and it was enacted with retroactive effect.¹¹⁸

The U.S Supreme court held that legislation violates due process where it is not rationally linked to a purpose that Congress sought to achieve when enacting such statute.¹¹⁹ The court held that the legislation was rationally connected to the purpose in the present matter as Congress sought to prevent employers from taking advantage and withdrawing whilst congress was still discussing the new Act.¹²⁰ Thus according to the finding by the court, the use of retroactive legislation was necessary and proper.¹²¹ The decision of the U.S Supreme court in *PBGC v. R. A. Gray & Co.*, portrays a view by the court that where it can be shown that there is a link between the legislation and the purpose then such legislation will not be declared invalid for being in conflict with due process.

In *United States v Carlton* the Respondent, Carlton, who was an executor of a will, decided to make use of a deduction that was available under a tax statute.¹²² He did so

¹¹⁵ *PBGC v. R. A. Gray & Co.*, 467 U.S. 717 (1984). [ONLINE] Available from: <https://supreme.justicia.com/cases/federal/us/467/717/>

¹¹⁶ *PBGC v. R. A. Gray & Co.* at p 717.

¹¹⁷ *PBGC v. R. A. Gray & Co.* at p 717.

¹¹⁸ *PBGC v. R. A. Gray & Co.* at p 717.

¹¹⁹ *PBGC v. R. A. Gray & Co.* at p 728.

¹²⁰ *PBGC v. R. A. Gray & Co.* at p729.

¹²¹ *PBGC v. R. A. Gray & Co.* at p729.

¹²² *United States v Carlton* 512 US 26 1994. [ONLINE] Available from: <https://www.supremecourt.gov>

by buying shares with estate funds and later selling the shares at a loss to an employee stock-ownership plan.¹²³ Carlton then claimed a deduction that had the effect of drastically reducing the estate tax liability.¹²⁴ Congress later enacted legislation that provided that in order to qualify for the deduction, the shares must have been owned by the deceased prior to his/ her death.¹²⁵ In addition, the amendment was to apply with retroactive effect and thus had the effect of disqualifying the transaction that Carlton entered into previously, from obtaining a deduction.¹²⁶

The Court held that the purpose of Congress when enacting the statute was neither arbitrary nor was it illegitimate therefore it was not in conflict with due process.¹²⁷ In addition, the court held that although Carlton relied on the law that prevailed at the time of concluding the transaction, that reliance alone is not sufficient to establish a constitutional violation.¹²⁸

Considering the two USA court decisions, it appears that the interpretation that is adopted by the courts requires only that the state should use a method that is connected to the result that the state seeks to achieve. Once this has been done by the state then the statutes whether retroactive or not will be acceptable to the courts. In both the *United States v Carlton and PBGC v. R. A. Gray & Co.* cases, the court based its decision on whether the legislation in question was rationally connected to the purpose for which it was enacted. It would therefore appear that the USA applies a low threshold in determining whether a statute is constitutional compared to South Africa. As a result, litigants will face a hurdle in persuading the court that a retroactive statute is unconstitutional as the test appears to favour the state over the individual taxpayers.

4.3 The United Kingdom

¹²³ *United States v Carlton* at p 28.

¹²⁴ *United States v Carlton* at p 28.

¹²⁵ *United States v Carlton* at p 29.

¹²⁶ *United States v Carlton* at p 29.

¹²⁷ *United States v Carlton* at p 32.

¹²⁸ *United States v Carlton* at p 33.

The United Kingdom does not have a supreme constitution, instead, parliament is sovereign and the laws passed by the legislature cannot be declared invalid by the courts.¹²⁹ The similarity between the UK and South Africa is that both are common law jurisdictions and this forms the basis for comparison. In the absence of a supreme constitution it is difficult for the judiciary to declare that legislation or conduct of the government is not in line with the constitution.¹³⁰ The courts can rulings to the effect that legislation or conduct of the government is not authorised or that it is unlawful.¹³¹ The test on the validity of retroactive fiscal legislation is therefore not whether it complies with the constitution, instead it is based on the lawfulness of such conduct.

The European Convention on Human Rights (ECHR) is an international treaty that imposes an obligation on states that are members or signatories of it to ensure that the people in their jurisdictions are afforded the rights contained in it.¹³² Countries that are signatories to the ECHR must afford protection to the rights of people in their jurisdictions as mandated by the ECHR and may not offer protection that is of a lower standard than that contained in the treaty.¹³³ The UK became a member of the ECHR in 1951, in addition, the UK enacted the Human Rights Act in 1993 in order to give effect to the ECHR.¹³⁴ The ECHR contains a prohibition against retroactive legislation in criminal law, however does not contain such a prohibition against retroactive statutes in the civil context.

In *Huitson v HMRC*, the appellant had entered into an agreement that resulted in the use of a double taxation treaty that existed and was entered into by the United Kingdom and the Isle of Man to avoid tax.¹³⁵ The effect of the agreement that the taxpayer entered into was that the taxpayer was only taxed on a smaller amount and the rest of his income that he received as a benefit from a trust was not taxable in the UK and it

¹²⁹ Parliament's authority. [ONLINE] Available from <https://www.parliament.uk/about/how/role/sovereignty/> [Accessed on 4-10-2018].

¹³⁰ Barend, E. 1998. *Constitutional law*, at p 30.

¹³¹ Barend, E. 1998. *Constitutional law*, at p 30.

¹³² Article 1 of the ECHR; Andreadakis, S. 2013. The European Convention on Human rights, the EU and the UK: Confronting a Heresy: A reply to Andrew Williams, 1187.

¹³³ Andreadakis, S. 2013. The European Convention on Human rights, the EU and the UK: Confronting a Heresy.

¹³⁴ Amos, M. 2017. The Value of the European Court of Human rights to the United Kingdom. *The European Journal of International Law*. 28(3), 763,764.

¹³⁵ *Huitson v HMRC* [2011] EWCA Civ 893 at par 3.

was also not taxable in the Isle of Man.¹³⁶ The legislature then introduced the Finance Act of 2008 retroactively, which closed the specific loophole that existed in legislation in the UK.¹³⁷

The appellant challenged the retroactive legislation on the basis that it violated his right to enjoy his property as contained in the First Protocol to the European Convention on Human Rights.¹³⁸ Among the grounds that were advanced for challenging the retroactive legislation, the appellant contended that it violated his legitimate expectation as a taxpayer and that it was against the principle of legality.¹³⁹

The court held that the enactment of fiscal legislation is within the powers of the state and that the state may impose legislation at its discretion having regard to the state of the economy.¹⁴⁰ Moreover the court stated that the legislation strikes a fair balance between the interests of the appellant and those of the other taxpayers.¹⁴¹ In effect the court expressed the view that legislation cannot be declared unlawful if it creates in a fair balance between the taxpayer concerned and the interests of the other taxpayers in the country.

In *St Mathews (west) v HMRC* the claimants were parties to an arrangement that had the effect of minimising their Stamp Duty Land Tax.¹⁴² Treasury became aware of the tax avoidance measures that flowed from the legislation that was in existence at that time; a new statute was then enacted by parliament with the effect of closing the loopholes that were used by the claimants to avoid tax.¹⁴³ The new statute was introduced with retroactive effect.¹⁴⁴ The claimants challenged the retroactive legislation on the basis that it violates their right to enjoyment of their property as contained in Article 1 Protocol 1.¹⁴⁵

¹³⁶ *Huitson v HMRC*, at par 15.

¹³⁷ *Huitson v HMRC*, at par 15.

¹³⁸ *Huitson v HMRC*, at par 2.

¹³⁹ *Huitson v HMRC*, at par 2.

¹⁴⁰ *Huitson v HMRC*, at par 95.

¹⁴¹ *Huitson v HMRC*, at par 95.

¹⁴² *St Mathews (west) v HMRC* [2014] EWHC 1848 (Admin), at par 2.

¹⁴³ *St Mathews (west) v HMRC* [2014] EWHC 1848 (Admin), at par 2.

¹⁴⁴ *St Mathews (west) v HMRC*, at par 15.

¹⁴⁵ *St Mathews (west) v HMRC*, at par 4.

The court held that any interference with the right to enjoyment of property must be lawful and proportionate.¹⁴⁶ The court referred to the earlier decision of *Huitson v HMRC* and re-affirmed that it is important that a balance be struck between the interests of an individual taxpayer and those of the community or other taxpayers.¹⁴⁷ The court then dismissed the claim and held that the challenged legislation was enacted for a good cause after the relevant factors were taken into account.¹⁴⁸

The fact that there is no supreme constitution in the United Kingdom means that legislation has to be challenged on other grounds instead of being measured against a supreme constitution. The litigants then rely on internal legislation and in other instances, on international treaties to assert their rights and seek relief from the courts. Retroactive taxation legislation is evidently an accepted manner of resolving defects in fiscal legislation in the United Kingdom. The Courts in *Huitson v HMRC* and in *St Mathews (west) v HMRC* held that the fair balance test is the means to measure whether legislation is lawful or not.

¹⁴⁶ *St Mathews (west) v HMRC*, at par 56.

¹⁴⁷ *St Mathews (west) v HMRC*, at par 60.

¹⁴⁸ *St Mathews (west) v HMRC*, at par 67.

4.4 Australia

The Australian legal system is similar to the South African legal system in that both are common law jurisdictions.¹⁴⁹ In addition, Australia has a Constitution which gives authority to the central government and the states to collect tax.¹⁵⁰ Section 5 of the Australian Constitution provides for the supremacy of the Constitution of Australia, that it prevails over all other laws and that the power to enact legislation flows from it.¹⁵¹ The existence of a supreme Constitution makes it less burdensome for taxpayers to assert their rights and challenge legislation, especially where the Constitution contains a bill of rights.

The Constitution of Australia does not contain a provision that prohibits the enactment of retroactive legislation, either implied or express.¹⁵² This means that parliament has the authority to enact legislation that has retroactive effect. Australia does not have express provisions that protect human rights in its Constitution.¹⁵³ The effect is that taxpayers are not able to rely on the Constitution to assert their rights and challenge legislation. In addition, the enactment of retroactive tax legislation is an accepted practice where the government has indicated its intention to do so by press release.¹⁵⁴

The Australian constitution does not prohibit the retroactive enactment of criminal legislation and this has been upheld by the Australian courts as being a proper legislative measure.¹⁵⁵ There is therefore little hope that the courts would in future find

¹⁴⁹ Brown, EF. 2010. A comparison of the handling of the financial crisis in the United States, the United Kingdom and Australia. *Villanova Law Review*, 55(3): 513.

¹⁵⁰ Ault, H & Arnold BJ. 2010. *Comparative income Taxation*, p 4.

¹⁵¹ Section 5 of the Australian Constitution.

¹⁵² Retrospective Laws. [ONLINE] Available at https://www.alrc.gov.au/sites/default/files/pdfs/publications/ip46_ch_7_retrospective_laws.pdf [Accessed on 11-10-2018].

¹⁵³ Ordower, H. Not dated. Restricting the Legislative Power to Tax: Intersections of Taxation and Constitutional Law: 1.

¹⁵⁴ Retrospective laws [ONLINE] Available at https://www.alrc.gov.au/sites/default/files/pdfs/publications/ir_127ch_9_retrospective_laws.pdf [Accessed on 4-10-2018].

¹⁵⁵ See *R v Kidman HCA 58 (1915)* and in *Polyukhovich v Commonwealth HCA 32 (1991)* where the courts in both cases found that retroactive criminal legislation is not unconstitutional and is acceptable.

that the enactment of retroactive taxation legislation is unlawful. Although Australia has a Constitution that is supreme, which is similar to South Africa and the USA, the Australian Constitution is different in that it does not protect the citizens and inhabitants of Australia from retroactive law-making in the criminal law field. This indicates the difficulty that a taxpayer would face in attempting to prove that a retroactive taxation statute is unlawful in Australia.

4.5 Conclusion

It appears that the acceptance of retroactive fiscal legislation is a thread that runs through all four jurisdictions, South Africa, UK, USA and Australia. The UK does not have a supreme constitution, the result of this is that taxpayers have to rely on international treaties and other internal legislation to challenge the lawfulness of retroactive taxation statutes.

The USA Constitution is similar to the South African Constitution as they both prohibit retroactive legislation in criminal law, however, no prohibition exists against retroactive civil or tax legislation.¹⁵⁶ Based on the *United States v Carlton and PBGC v. R. A. Gray & Co.* it is clear that in the USA, retroactive tax legislation that is rationally connected to its purpose is likely to pass the constitutionality muster. This is a very low threshold and it imposes an onerous burden on taxpayers who wish to challenge a retroactive statute.

In Australia, the test is whether retroactive legislation is lawful or not, instead of whether it is constitutional, this is because of the lack of a bill of rights in the Australian Constitution. As highlighted above, this creates hardships for taxpayers who want to challenge the constitutionality of retroactive fiscal statutes. Overall, the three foreign jurisdictions are accepting of retroactive fiscal legislation even if it leads to the taking away of property from taxpayers. The distinguishing factor for South Africa is section 36(1)(e) of the Constitution which requires that where there are less restrictive means that can be applied to limit a right in the bill of rights then such means should be

¹⁵⁶ Neuhoff, RR. 1935. Retrospective Tax Laws at p 1; Section 35 (3) (l) of the Constitution.

employed. This view is supported by Croome.¹⁵⁷ None of the three mentioned countries have a similar provision in their constitutions or in their approaches to the enactment of retroactive statutes. The court in the South African *FNB* case laid down principles that are similar to the 'fair balance' approach that was set out in the *Huitson v HMRC*¹⁵⁸ and in *St Mathews (west) v HMRC*.¹⁵⁹ This approach should be retained in South Africa and used in conjunction with the test that is laid out in section 36 of the South African Constitution as it more likely to produce outcomes that are more equitable.

¹⁵⁷ See n105 above.

¹⁵⁸ *Huitson v HMRC* [2011] EWCA Civ.

¹⁵⁹ *St Mathews (west) v HMRC*.

Chapter 5: Conclusion

The overall purpose of this study was to investigate whether retroactive tax legislation is in line with the Constitution. This research was also aimed at investigating the relationship between retroactive legislation and the rule of law. It was also the purpose of this study to analyze the manner in which Australia, the United Kingdom and the United States of America approach retroactive legislation. This was based on the fact that these three foreign jurisdictions, like South Africa, are common law jurisdictions and two of them have supreme Constitutions.¹⁶⁰ An investigation into how they deal with the concept of retroactive legislation was considered essential to determine if the practice in South Africa aligns with the practice in other countries.

Chapter 2 of this research discussed the rule of law as a value that underlies the Constitution and that it should be taken into consideration when determining whether legislation or conduct is in line with the Constitution.¹⁶¹ This chapter also discussed legal certainty as a characteristic of the rule of law and it went on to show that the imposition of retroactive tax legislation offends the principle of legal certainty. The reason for this assertion is that retroactive tax legislation deprives individuals of the opportunity to predict the outcomes of their conduct and plan accordingly.

The role of the legislature and that of the judiciary has been discussed in chapter 2 of this research. This paper has shown that although the legislature has the authority to enact legislation, such authority must be exercised in a manner that conforms to the Constitution. The judiciary is there as a last resort for the individuals who are aggrieved by the conduct of organs of state, and it possesses the power to intervene when organs of state act in a manner that is contrary to the Constitution. This research has shown that it appears that the enactment of retroactive taxation legislation is not an issue that is considered by the judiciary to be a violation of the rule of law. This assertion is based

¹⁶⁰ Brown, EF. 2010. A comparison of the handling of the financial crisis in the United States, the United Kingdom and Australia. *Villanova Law Review*, 55(3): 513.

¹⁶¹ Section 1(c) of the Constitution.

on the decision of the High Court in the *Pienaar Brothers*¹⁶² case which has been discussed above.

Chapter 3 discussed the right to property, and it went on to show that legal scholars and courts have provided guidance with regards to a proper interpretation of what constitutes property in the constitutional sense. This chapter further discussed and conclusively showed that the enactment of retroactive fiscal legislation amounts to an interference with the property of the taxpayers, property being money in this case. In addition, this chapter has detailed how the retroactive tax legislation amounts to an arbitrary deprivation of property.

The court's ruling in the *Pienaar Brothers*¹⁶³ case could have set a precedent that leads to the protection of the rights of the taxpayers, however that opportunity was missed. The legislature has the option of enacting legislation that operates prospectively to ensure that the existing rights of the taxpayers are not destabilized, instead of enacting retroactive legislation that has adverse financial consequences for the taxpayers. The *Pienaar Brothers*¹⁶⁴ case unfortunately displays a situation where both the legislature and the judiciary failed to properly consider and protect the rights of the South African taxpayers.

Chapter 4 outlined that South Africa, the United Kingdom, the United States of America and Australia, all display an acceptance of retroactive fiscal legislation. The absence of a single codified Constitution in the UK results in taxpayers having to rely on international treaties and other internal legislation to challenge the lawfulness of retroactive tax legislation. This chapter also discussed the USA Constitution, particularly its similarity to the South African Constitution in that they both prohibit retroactive legislation in criminal law and that no prohibition exists against retroactive civil or tax legislation in both of these constitutions.¹⁶⁵ Based on the *United States v Carlton and PBGC v. R. A. Gray & Co.* it is clear that in the USA, retroactive tax legislation that is

¹⁶² *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service and Another.*

¹⁶³ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service and Another.*

¹⁶⁴ *Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service and Another.*

¹⁶⁵ Neuhoff, RR. 1935. Retrospective Tax Laws at p 1; Section 35 (3) (l) of the Constitution.

rationality connected to its purpose is likely to pass the constitutionality muster. This is regardless of the detriment that is suffered by the taxpayer as a result thereof.

It has been shown in the above discussion of the Australian legal system that the test in Australia is whether retroactive legislation is unlawful or not, instead of whether it is constitutional. This is because there is no bill of rights in the Australian Constitution. Overall, the three foreign jurisdictions are accepting of retroactive fiscal legislation even if it leads to the taking away of property rights from taxpayers. South Africa is different from the three foreign jurisdictions because of section 36(1)(e) of the Constitution which requires that where there are less restrictive means that can be applied to limit a right in the Bill of Rights then such means should be employed.¹⁶⁶ This provision is not available in any of the three foreign jurisdictions and it may justify a contention that the legislature should rather close loopholes in legislation prospectively instead of doing so retroactively.

¹⁶⁶ The Constitution of the Republic of South Africa, 1996.

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